No. 20776

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

UNITED STATES AND THE NATIONAL AERONAUTICS AND SPACE ADMINISTRATION,

Appellants,

vs.

PHYSICS TECHNOLOGY LABORATORIES, INC., *et al.*,

Appellees.

Appeal From the United States District Court for the Southern District of California Southern Division.

BRIEF FOR APPELLEES.

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*Erroneously referred to herein as Pabloc.

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BRIEF FOR APPELLEES.

Jurisdictional Statement.

Appellees agree with the Jurisdictional Statement of Appellants.

Statement of the Case.

Appellees do not controvert the Statement of the Case of appellants except that it does not agree with the Government's position (Appellants' Br. p. 4).

Statutory Provisions.

Appellees agree that appellants have correctly cited and quoted the statutory provisions involved.

Question Presented.

Appellees believe that appellants' statement of "Questions Presented" (Appellants' Br. pp. 7-8) inaccurately

presents the real question involved. Appellees would state it thusly:

Does an action to recover damages by reason of the "negligent and/or wrongful acts and omissions of" Government (NASA) employees in disclosing appellees' "secret and confidential . . . trade secret . . . and proprietary right" [R. 25, *et seq.*][1] to persons (competitors of appellees) outside Government arise *ex contractu* and, therefore, establish jurisdiction in the United States Court of Claims under the Tucker Act, [28 U.S.C. 1491], or does it arise *ex delicto* and, therefore, establish jurisdiction in the United States District Court under the Federal Tort Claims Act [28 U.S.C. 1346(b)]?

Argument.

Appellees' Amended Complaint [R. p. 25, *et seq.*] alleges, among other things, "At all times involved herein, NASA, its officers and employees while acting within the scope of their office or employment, received and accepted said concept to consider, study, keep, hold and retain on a secret and confidential basis." Seizing upon this language and ignoring the other allegations of the complaint, appellants would have this Court believe that the Government and appellees entered into a contract to keep the secret. This is far from the facts of the case.[2] This allegation should be construed in light of the other allegations of the amended complaint to mean what it states and nothing more—certainly *not* that it establishes a contractual relationship between the parties.

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[1]Record references are indicated thusly: "R. p. .....".

[2]Appellees refer to language in the original complaint using the word "agreed" (eliminated in the Amended Complaint) to bolster their claim of "contract" (Appellants' Brief, p. 4).

There was no contract within the meaning of 28 U.S.C. §1491 (as amended) which provides, "The Court of Claims shall have jurisdiction to render judgment upon any claim against the United States founded either upon the Constitution, or any Act of Congress or any regulation of an executive department, or upon any express or implied contract with the United States, or for liquidated or unliquidated damages in cases *not sounding in tort*" (emphasis supplied). The jurisdiction of the Court of Claims upon any express or implied contract with the United States means actual contracts, either express or implied in fact.[3] *State of Alabama v. United States* (1931), 282 U.S. 502. The Court of Claims has jurisdiction of all actions *ex contractu* but not of actions *ex delicto, Ingram v. United States* (1897), 32 Ct. Cl. 147, reversed on other grounds 172 U.S. 327. The liability of the Government in actions on contract, is simply that which the claimant might pursue against another defendant in another Court, *Deming v. United States* (1865), 1 Ct. Cl. 190, appeal dismissed 76 U.S. 145.

Appellees' claims in this case are not based on any contract expressed or implied but rather on a tort—breach of confidence—which in this case is founded on the common-law tort of breach of confidence, the violation of the statute 18 U.S.C. §1905 and the violation of the regulations of appellants,[4] any one or all of which

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[3]The phrase "not sounding in tort" prevents a claimant from waiving a tort and suing *ex contractu*, even in a case where he could have done so at common law. *McArthur v. U.S.* (1894), 29 Ct. Cl. 194. See, also, *Castelo v. U.S.* (1916), 51 Ct. Cl. 221.

[4]As to regulations concerning disclosure of confidential information, trade secrets and proprietary data, see Armed Service Procurement Regulations 4-205.1e and Title 41 C.F.R. 18-3, 109(a).

constitutes the negligent and/or wrongful acts and omissions of appellants within the meaning of 28 U.S.C. §1346(b).

We have no quarrel with the basic proposition of appellants that breach of contract claims against the United States are within the jurisdiction of the Court of Claim under 28 U.S.C. §1491, (except claims involving not more than $10,000 [28 U.S.C. §1346(a)(2)] and that the cases cited by appellants support this basic proposition.[5]

Fulmer v. United States, 83 Fed. Supp. 137 (1949), a decision of the United States District Court for the Northern District of Alabama, Southern Division, involved a claim by plaintiff that the United States "would pay to plaintiff for the use of said device, invention, means or method, the reasonable value of same" and contemporaneously therewith agreed that plaintiff's "disclosure would be treated in confidence, that such disclosure would not be revealed to the public or otherwise be appropriated." (83 Fed. Supp. 138).

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[5]We do not agree, however, that the decision of the District Court for the Northern District of Alabama, Southern Division, in the *Fulmer v. U.S.*, 83 Fed. Supp. 137 (1949) is sound in its entirety. For example, Fulmer appears to decide that where plaintiff's alleged invention had never been patented, he could not maintain an action against the United States under the Federal Tort Claims Act for damage to or loss of his "property" since an unpatented invention is only an inchoate right and in the absence of statute, no suit can be maintained for using it before the patent is issued. To the contrary, the United States Court of Appeals for the District of Columbia, *Aktiebolaget Bofors v. U.S.*, 194 F. 2d 145 (1951) held that the owner of an unpatented trade secret has a proprietary right in it so long as he does not disclose it and his right to exclusive use of it depends upon continuance of secrecy. (194 F. 2d 147), quoting from the opinion of Judge Holtzoff in the decision below, "So long as the secret remains intact, anyone who invades it is guilty of a tortious act". (*Aktiebolaget Bofors v. U.S.* (D.C. 1950), 95 Fed. Supp. 131, 133).

The *Fulmer* case clearly involved a claim of a *contract* between plaintiff and the Government "express or implied." This action does not involve such a claim. Furthermore, as pointed out, *infra,* the cases cited by appellants all involve a breach of a duty *created by and arising out of contract,* whereas the cause of action alleged in appellees' Complaint involves the breach of a duty to retain a confidence arising out of a *relationship of confidence and trust.*

The *Bofors* case, *supra,* cited by appellants involved a *contract* between the United States and Aktiebologet Bofors by the terms of which Bofors granted to the Navy Department, in consideration of the sum of $600,000, an "Exclusive and irrevocable license to make, use and have made in the United States for the United States use the Bofors 40 mm. water-cooled gun. . . .". Bofors also agreed under the contract to make full disclosure of its secret process and to furnish the services of two expert production engineers for a period of one year. Bofors based its claim under the Federal Tort Claims Act on the "transfer, under the Lend Lease Act and similar legislation, Bofors guns and ammunition to other nations to be used by them in the common war against Germany and Japan". (194 F. 2d 147). The Circuit Court for the District of Columbia held that the claim stated in the complaint was one for "breach of the licensing agreement"; "a tort claim was not stated in the Complaint"; and "it should be borne in mind that the purpose of the action was not to prevent unlicensed use of the trade secret . . . but to obtain compensation for past and future use of the secret beyond the scope of the license which had been granted" (194 F. 2d pp. 148-149).

It is important also to note that as pointed out by appellants in their Brief (pp. 17-18), a successful action against the United States was maintained by Aktiebolaget Bofors Company in the Court of Claims for *breach of contract* (Appellees' Memo. p. 11).

Appellants' Brief also cites *Pabloc Co. v. U.S.,* 161 Ct. Cl. 369, 137 U.S.P.Q. 224 (Ct. Cl. 1963). This case involved a claim by plaintiff that a contract between plaintiff and the Government had been consummated under the terms of which the Government would designate plaintiff's package for fire bombs as the only approved alternate to a Chemical Corps package on future procurements until 104,000 packaged fire bombs had been delivered to (or ordered by) the Government, whereupon plaintiff would grant the Government a royalty-free license under its patents, plus "know-how". Meanwhile, plaintiff would supply the Government with drawings, specifications and "know-how" for inspection purposes. Almost immediately after this proposal had been stated and signed by plaintiff (although not signed by the Government), the Government amended an existing bid invitation to designate plaintiff's package as the approved alternate unit. Not long thereafter, it was determined by the Government that the Chemical Corps package did not meet the Government's performance requirements while plaintiff's did. Whereupon, the Government had plaintiff's drawings copied and given to other fire bomb contractors together with other information obtained from plaintiff. As a result, the other contractors manufactured the package. The Government

argued that nothing more than an unilateral offer was contemplated and that there was no countervailing promise by the Government. (Plaintiff sought damages for violation of contract and also sought compensation for the unlicensed use of patents which were the subject of the contract). The Court of Claims found "the contract count decisive" and, in addition, held that as a part of that agreement the Government had promised to abide by plaintiff's condition that its trade secret including "know-how" would not be disclosed to anyone outside of Government until after the delivery to (or order by) the Government of 104,000 fire bombs in plaintiff's package, and ordered the case to proceed before the Trial Commissioner for the determination of damages.

It should be crystal clear that the cases cited by appellants in their memorandum (while supporting a valid proposition that claims against the United States arising out of contract, express or implied, and which are "essentially for breach of a contractual undertaking" are exclusively within the jurisdiction of the Court of Claims (if over $10,000)), are relied on by appellants in the mistaken idea of what is actually involved in this case and are completely irrelevant to the issues pleaded in the Amended Complaint. We believe that our discussion of those cases in light of the allegations of appellees' Amended Complaint here and in light of the provisions of the Federal Tort Claims Act, unerringly demonstrates that a cause of action within the jurisdiction of the District Court has been pleaded.

Appellees' Tort Claim.

Appellees' claim in this action, as we have pointed out, is based solely upon an alleged tort committed by defendants, its officers and employees while acting within the scope of their office and employment, "under circumstances where the United States, if a private person, would be liable to the appellees in accordance with the law of the place where the acts and omissions alleged by appellees occurred". (28 U.S.C. §1346.)[6] Appellees claim that appellants committed "negligent and/or wrongful acts and omissions" which are cognizable under the law of torts on three bases:

1. The violation of the common law duty to retain the trade secret and proprietary right of plaintiffs in confidence;
2. The violation of the statutory duty not to publish, divulge or disclose trade secrets under penalty of criminal sanctions (18 U.S.C. §1905); and
3. The violation of the duty imposed by Government regulations not to disclose confidential information, trade secrets and proprietary rights under Armed Services Procurement Regulations 4-205.1e and Title 41 C.F.R. 18-3, 109(a).

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[6]Appellants, in their Brief (p. 10) complain: ". . . if the District Court's ruling is permitted to stand as precedent, not only will the federal departments and agencies be subject to the differing laws of the fifty states in handling trade secrets, but also the trade secret owner will be permitted to choose both his forum, Court of Claims or the district courts, and the law to be applied, federal law or state law. This would clearly be an anomalous result." Under the Federal Tort Claims Act, are not federal departments and agencies subject to the differing laws of the fifty states concerning Negligence, Master and Servant, etc.? Furthermore, in tort cases, there is only one forum—the United States District Court.

Appellees claim that the violations by appellants of each of their duties to appellees referred to above constituted negligent and/or wrongful acts or omissions within the meaning of 28 U.S.C. §1346 and proximately caused injury or loss of property to appellees for which they seek money damages.

As stated by appellants in their Brief (p. 9, fn. 2) their common law duty to retain the trade secret or proprietary right of appellees in confidence is clearly expressed in Restatement of Torts §767 which provides as follows:

Liability for Disclosure or Use of Another's Trade Secret—General Principle

> "One who discloses or uses another's trade secret, without privilege to do so, is liable to the other if (a) he discovered the secret by improper means, or (b) his disclosure or use constitutes a breach of confidence reposed in him by the other in disclosing the secret to him. . . ."

Concerning clause (b), the Restatement comments:

> "A breach of confidence under the rule stated in this clause may also be a breach of contract which subjects the actor to liability under the rules stated in the Restatement of Contracts. But whether or not there is a breach of contract, the rule stated in this Section subjects the actor to liability if his disclosure or use of another's trade secret is a breach of the confidence reposed in him by the other in disclosing the secret to him. The chief example of a confidential relationship under this rule is the relationship of principal and agent . . . But this confidence may exist also in other situations. For ex-

> ample, A has a trade secret which he wishes to sell with or without his business. B is a prospective purchaser. In the course of negotiations, A discloses the secret to B solely for the purpose of enabling him to appraise its value . . . [In such a case] B is under a duty not to disclose the secret or use it adversely to A."

To emphasize that the duty not to disclose appellees' secret may arise as a matter of tort law rather than out of a contract, the Restatement of Torts in a subsequent comment appearing in §767 states that (such) "duty not to disclose may arise out of a contract made by him *or it may be based on the rules stated in Clauses (a), (b) and (d)*[7] *of this Section.*"

The facts as alleged in appellees' Amended Complaint fall squarely within the example described in the preceding "Comment on Clause (b)": "A (Appellants) has a trade secret (Propulsion by Sputtering Concept) which he wishes to sell with or without his business. B (NASA and the United States Government) is a prospective buyer. In the course of negotiations (submission of proposals), A (Appellees) discloses the secret to B (Government and NASA) solely for the purpose of enabling him (Government and NASA) to appraise its value."[8]

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[7]"(d) he learned the secret with notice of the facts that it was a secret and that its disclosure was made to him by mistake."

[8]Parenthetical matters supplied.

The Law of Ohio.

Appellees bring their action and invoke the jurisdiction of this Court under the Federal Tort Claims Act. Having established jurisdiction, to prove their case, appellees need but establish that the cause of action set forth in their Amended Complaint involves negligent and/or wrongful acts which constitute a tort for which the Government, if a private person, would be liable under the law of the state in which the act or omission complained of occurred (and that said tort proximately caused injury or loss of property to appellees, and the money damages flowing therefrom). The act or omission complained of occurred at the Lewis Research Center, Cleveland, Ohio. The act or omission complained of is the wrongful and/or negligent disclosure in the state of Ohio by the officers and employees of NASA and the U. S. Government of a confidence responded in them by appellees (while acting within the scope of their office or employment). Ohio law recognizes the existence of a confidential relationship not arising out of contract: "A confidential relationship may be said to exist whenever trust and confidence is reposed by one person in the integrity and fidelity of another." *State ex rel. Shriver v. Ellis* (App.), 49 O.L. Abs. 161, 75 N.E. 2d 704 (1947). "It may be natural or defacto or legal and formal". *Taylor v. Shields* (App.), 64 O.L. Abs. 193, 111 N.E. 2d 595. "The relationship of confidence and trust . . . is not confined to those well-known relations of trustee and beneficiary, guardian and ward, and attorney and client. It applies to every case where . . . confidence is reposed and betrayed." *Smith v. Patterson*, 33 O.S. 70. See also discussion and cases collected in 23 Ohio Jur. 2d 539, *et seq.*

Ohio law recognizes the existence of a trade secret as a property right and provides for its protection against invasion by breach of trust. *Owens Mach. Co.* (App.), 10 O.L. Abs. 367. Ohio Courts will enjoin the disclosure of a secret mechanical idea, the knowledge of which was obtained in confidence. *Recording and C. Mach. Co. v. Neth,* 7 ONP NS 217, 19 ODNP 169, 80 N.E. 1129. See also discussion and cases collected in 52 Ohio Jur. 2d 417, *et seq.* Thus, we see that Ohio law recognizes and confirms the existence of the tort described in subparagraph (b) of §757 of Restatement of Torts.

Ohio also acknowledges that the violation of a specific criminal statute or ordinance may be the basis for a civil claim for damages and may constitute negligence *per se.* Under Ohio law, appellees need but prove the appellants' violation of §1905 of Title 18, United States Code in order to establish appellants' negligence as a matter of law. "Negligence *per se* is a violation of a specific requirement of law or ordinance, the only fact for determination by the jury being the commission or omission of the specific act inhibited or required." "Conduct violative of specific legislative requirement is illegal, and if it proximately results in injury to one to whom the duty is owed, the transgressor is liable for the resulting damage." See discussion and cases collected in 39 Ohio Juris. 2d 550, *et seq.*

Woodbury v. United States.

Appellants rely most heavily on the decision of this Court in *Woodbury v. United States,* 313 F. 2d 291 (C.A. 9, 1963). This case was held to involve a cause of action for *breach of a contractual undertaking* and any

action, if maintainable, must be brought in the Court of Claims under the Tucker Act.

This case involved a claim by plaintiff (and the trial court so held (192 Fed. Supp. 924) that in connection with the "contractual obligation" to provide financing for the construction of a housing project there existed "an implied obligation of HHFA (Housing and Home Finance Agency) to arrange for or provide long-term financing, and that it did not do so" (313 F. 2d 294). Plaintiff asserted a contract (within HHFA's contractual obligations to him) not "express", but "implied". Plaintiff termed it a breach of HHFA's fiduciary duties. The United States District Court for the District of Oregon dismissed the action for lack of jurisdiction holding that if there was a breach of fiduciary duties, such a breach was not the "ordinary common-law type of tort" contemplated by the Federal Tort Claims Act (313 F. 2d 294). On appeal, it was argued by appellant that breach of fiduciary duty is a tort "even though the duty may be created by contract". This Court stated with regard to this argument, "We assume, for the purposes of this decision, but do not decide, that these arguments are sound as far as they go." A number of cases are cited in support of the proposition that the coverage of the Federal Tort Claims Act is not limited to the "ordinary common-law type of tort". We have no quarrel with them, but we are still of the view that appellant does not have a case under the Act" (313 F. 2d 294-295). This Court pointed out that jurisdiction of the courts over contract claims against the Government is different from jurisdiction over tort claims. The first is lodged in the Court of Claims under 28 U.S.C. §1491 and the second, in the

United States District Courts under 28 U.S.C. §1346-(b). This Court also pointed out that the law to be applied in construing or applying provisions of Government contracts is federal and the law to be applied under the Federal Tort Claims Act is state (313 F. 2d 295). The Federal Tort Claims Act expressly provides for liability of the United States for torts "under circumstances where the United States, if a private person, would be liable to the claimant in accordance with the law of the place where the act or omission occurred" [28 U.S.C. §1346(b)].

This Court stated,

> "Many breaches of contract can also be treated as torts. But in cases such as this where the tort complained of is based *entirely* upon breach by the Government of a promise made by it in a contract, so that the claim is in substance a breach of contract claim, and only incidentally and conceptually also a tort claim, we do not think that the common law or local state law right to waive the breach and sue in tort brings the case within the Federal Tort Claims Act" (Emphasis supplied, 313 F. 2d 295).

This Court carefully pointed out,

> "We do not mean that no action will ever lie against the United States under the Tort Claims Act if a suit could be maintained for a breach of contract based upon the same facts. We only hold that where, as in this case, the action is essentially for breach of a contractual undertaking, and the liability, if any, depends wholly upon the Government's alleged promise, the action must be under the Tucker Act and cannot be under the Federal Tort Claims Act. . . . Fiduciary duty or not, there

> can be no liability in this case unless Woodbury can prove (1) an express or implied promise by the Government, through HHFA, to adopt and carry out a promised long-range plan to finance the project and (2) a wrongful breach of that promise" (313 F. 2d 296-297).

The following statement appearing in the penultimate paragraph in the Court's decision is enlightening,

> "Since it appeared in oral argument that Woodbury also has a case pending in the Court of Claims, the case being held in abeyance pending our decision, we see no need for transferring this case to that court under 28 U.S.C. §1406(c)."

The *Woodbury* decision carefully explains that "the law to be applied in construing or applying provisions of government contract is federal, not state law" and that, under the Federal Tort Claims Act, "state law, not federal law, controls" (313 F. 2d 295). There, appellant argued, ". . . that breach of fiduciary duty is a tort, even though the duty may be created by contract . . ." (313 F. 2d 294).

This Court points out,

> "The notion of such waiver of breach and suit in tort is a product of the history of English forms of action; it should not defeat the long established policy that government contracts are to be given a uniform interpretation and application under federal law, rather than being given different interpretations and applications depending upon the vagaries of the laws of fifty different states." (313 F. 2d 295).
>
> "Allowing the plaintiff to waive the breach and sue in tort would destroy the distinction between

> contract and tort preserved in the federal statutes. As the Supreme Court said in Feres, supra, at 139, 71 S.Ct. at 156, the Tort Claims Act 'should be construed to fit, so far as will comport with its words, into the entire statutory system of remedies against the Government to make a workable, consistent and equitable whole.' It has been repeatedly held that one having a claim against the government that is essentially one sounding in tort may not 'waive the tort and sue in assumpsit,' thereby bringing his claim under the Tucker Act as one upon a contract with the United States, even though he could have done so under local law if he were asserting the same claim against a private party." (313 F. 2d 296).

It should be beyond question upon reading the allegations of the Amended Complaint [R. p. 25, *et seq.*], in their entirety that appellees' claim is not based "entirely" or even partly "upon breach by the Government of a promise made by it in a contract" (313 F. 2d 295). *No contract (express or implied) with the Government is involved.* And, appellants cannot distort the language of a single phrase taken out of context to create one. As in the case of *Aleutco Corporation v. United States* (C.A. 3, 1957, 244 F. 2d 674, 678-679) cited and discussed by this Court in the *Woodbury* case (313 F. 2d 296-297) this is a "classic case in tort."

The case of *United States v. Smith* (C.A. 5, 1963, 324 F. 2d 622), discussed by appellants in relation to the *Woodbury* decision (Appellants' Br. pp. 29-30) is not in point. There, six subcontractors who performed work for a Government prime contractor, sued the United States under the Federal Tort Claims Act on the

ground that the Government contracting officers failed to require a payment bond from the contractor under the Miller Act, 40 U.S.C. §270a, before execution of the prime contract. The absence of such payment bond made it impossible for the subcontractors to collect for the materials and labor furnished by them on the job. The trial court held that the failure of the contracting officers for the Government to obtain such bond violated the Miller Act.

Concerning the alleged violation of the Miller Act, the 5th Circuit held, "We do not need to decide whether the Miller Act placed on the United States Government a duty to the supplier of labor and materials in a public contract to see to it that the bond required of the contractor be executed prior to the letting of the contract . . ." (324 F. 2d 624).

The Court concluded,

> "We think that it (the Federal Tort Claims Act) indicates clearly that Congress did not intend to permit the suit against the United States for the contract price of a construction project remaining unpaid by the contractor merely because under the laws of some of the states, a state or municipality might be subject to such liability for the protection of such unpaid creditors on state public contracts."

The Court then cited and quoted from the *Woodbury* case, including the statement,

> ". . . where the 'tort' complained of is based entirely upon breach by the Government of a promise made by it in a contract, so that the claim is in substance a breach of contract claim, and only incidentally and conceptually also a tort claim, we

> do not think that the common law or state law right to waive the breach and sue in tort brings the case within the Federal Tort Claims Act."

It may be noted that appellants, after twisting and torturing the single phrase of the Amended Complaint referred to, *supra.* p. 2, in trying to emphasize the importance of a decision here, state:

> "NASA has over 30,000 employees located at major research installations throughout the country. Over 12,000 of these employees are scientists and engineers who may be called upon from time to time to review and evaluate a *potential contractor's* trade secret or proprietary information submitted *in hope of being awarded a NASA contract.* NASA officials estimate that during fiscal year 1965 alone over 3,000 *unsolicited proposals* were submitted by private concerns to NASA for evaluation." (Emphasis supplied, App. Br. pp. 30-31).

This is precisely the status of appellees. They were a *potential contractor;* they had submitted their trade secret and proprietary right in the form of an *unsolicited proposal in hope of being awarded a NASA contract.* Appellees were *not awarded a NASA contract.* NASA tortiously disclosed their trade secret and proprietary right.

It is respectfully submitted that the Order of the District Court should be affirmed.

Dated: September 12, 1966.

GEORGE W. JANSEN,
RICHARD M. RAND,
Attorneys for Appellees.

Certificate.

I certify that in connection with the preparation of this brief, I have examined Rules 18 and 19 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those Rules.

RICHARD M. RAND